In the Matter
of
THE WESTERN PACIFIC RAILROAD CO.
a Corporation, *Debtor*

FREDERICK H. ECKER, et al,
Petitioners,
against
WESTERN PACIFIC RAILROAD CORPORATION, et al,
Respondents.
No. 2

CROCKER FIRST NATIONAL BANK
OF SAN FRANCISCO, et al,
Petitioners,
against
WESTERN PACIFIC RAILROAD CORPORATION, et al,
Respondents.
No. 3

RECONSTRUCTION FINANCE CORPORATION,
Petitioner,
against
WESTERN PACIFIC RAILROAD CORPORATION, et al,
Respondents.
No. 30

BRIEF OF THE RAILROAD CREDIT CORPORATION, *Respondent*

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Baltimore, Maryland
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QUINN & BODEN PRESS, INC., NEW HAVEN, CONN.

Supreme Court of the United States

OCTOBER TERM, 1942

In the Matter

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THE WESTERN PACIFIC RAILROAD CO.,
a Corporation, *Debtor*

FREDERICK H. ECKER, et al, *Petitioners,* against WESTERN PACIFIC RAILROAD CORPORATION, et al, *Respondents.*	No. 7
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BRIEF OF THE RAILROAD CREDIT CORPORATION, *Respondent*

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Five petitions for writs of certiorari to revie the decree of the United States Circuit Court of Appeals for the Ninth Circuit entered November 28, 1941, were filed with and allowed by this Court on April 27, 1942. In addition, a Memorandum was also filed by the Interstate Commerce Commission, through the Solicitor General, as *amicus curiae*, urging this Court to grant the petitions for writs of certiorari in these cases in order that the Commission's duties under Section 77 and the procedure to be followed and the findings to be made by it in preparing and certifying future plans of reorganization may be established by a definite decision of this Court.

OPINIONS BELOW

The opinion of the United States Circuit Court of Appeals for the Ninth Circuit, from which these several petitions for review on writs of certiorari were filed, was rendered on November 28, 1941, and is officially reported in 124 F. (2d) 136, (R. 2663). This opinion reversed the decree of the District Court which approved *in toto* the plan of reorganization certified to it by the Interstate Commerce Commission pursuant to Section 77(d) of the Bankruptcy Act (11 U. S. C. A. § 205) and is officially reported in 34 F. Supp. 493 (R. 1569 to 1600).

JURISDICTION

The jurisdiction of this Court is invoked under Section 240-a of the Judicial Code, as amended by Act of Con-

gress of February 13, 1935 (U. S. Code, Title 28, Section 347-a) and §24(c) of the Bankruptcy Act (11 U. S. C. § 47(c)).

SUMMARY OF ARGUMENT

Pursuant to the provisions of Rule 27(d) and subdivision 4 thereof of the Rules of this Court, respondent leaves to counsel for petitioners to include in their briefs a concise statement of the case. For purposes of clarity, however, and to facilitate an immediate understanding of the reasons upon which this respondent based its objections to the treatment recommended for its claim in the Commission's plan and approved by the District Court, a brief statement of the claims of the collaterally secured noteholders, *i.e.*, The Railroad Credit Corporation, the Reconstruction Finance Corporation and the A. C. James Company, is recited.

Before proceeding to a discussion of this matter and a summary of the argument, it is appropriate at the outset to advise the Court that this brief will be confined and limited to a discussion of only two of the Statement of Points upon which it relied on its appeal to the Circuit Court of Appeals. Said two points, Nos. 6 and 7, (R. 1644) are is follows:

> "6. The District Court has erred in approving a plan of reorganization which treats the claim of the Reconstruction Finance Corporation upon a different basis with respect to the collateral securing that claim than similar claims of The Railroad Credit Corporation and the A. C. James Company to the extent that they are secured by the same or similar collateral.
>
> "7. The limitation on capitalization fixed in the Plan approved by the District Court does not constitute a valuation or appraisal of the Debtor's property, including the actual investment therein, such as is required by Section 77 of the Bankruptcy Act, as Amended, and the law of the land."

This limitation of argument is to avoid repetition and because pertinent objections raised by this respondent in the Court below are substantially similar to those of other respondents whose arguments will be adequately presented in their briefs. Therefore, The Railroad Credit Corporation (hereinafter referred to as R. C. C. or Credit Corporation) hereby concurs in and adopts as its own the briefs and arguments presented by the other respondents in support of the other objections to the plan raised in the District Court and argued in the Court below.

ARGUMENT

POINT ONE

The District Court has erred in approving a plan of reorganization which treats the claim of the Reconstruction Finance Corporation upon a different basis with respect to the collateral securing that claim than similar claims of The Railroad Credit Corporation and the A. C. James Company to the extent that they are secured by the same or similar collateral.

It is urged in the brief filed on behalf of A. C. James Co., respondent, that the secured claims of The Railroad Credit Corporation, Reconstruction Finance Corporation and A. C. James Co. should be recognized and refunded in full, and upon the same basis, both because the property of the debtor is sufficient in value to cover fully these three claims and because the property on which the General and Refunding Mortgage of the debtor constitutes a prior lien is sufficient in value to require that the claims of the creditors secured thereby should be refunded in full. The Railroad Credit Corporation expressly adopts and reaffirms this argument. While the Credit Corporation objects herein to the preference accorded to Reconstruction Finance Corporation and

insists that the allocation of securities between the Credit Corporation, Reconstruction Finance Corporation and A. C. James Company, as proposed in the Commission Plan, cannot be justified in law, even upon the assumption that the Commission's capitalization can be sustained, this petitioner again urges that the value of the debtor's property is sufficient to justify capitalization of at least $120,000,000, and it is sufficient in amount to require the refunding in full of all secured claims.

Claims of the Collaterally Secured Noteholders.

1. The Railroad Credit Corporation:

This respondent is a claimant in these reorganization proceedings by reason of two collaterally secured loans made to The Western Pacific Railroad Company—now the Debtor. Said loans were made on June 29, 1932, in the sum of $1,303,000 and on March 25, 1933, in the amount of $1,293,439, being due and payable on February 28, 1934, and March 24, 1935, respectively. Although the two promissory notes evidencing these loans have fixed maturity dates, nevertheless, they are in terms callable on demand, in the absence of which they are due and payable on their respective maturity dates. These notes carry the interest rate of the Federal Reserve Bank in New York City, which is presently 1% and has been such since October 1, 1937. The following items of collateral are pledged as security for both obligations: (R. 1577(b)).

(a) $4,000,000 Debtor's General and Refunding Bonds, Series A and B. ($2,000,000 of these bonds, Series A, were actually pledged with and delivered to the Credit Corporation by the A. C. James Co.).

(b) All right, title and interest of The Western Pacific Railroad Corporation in and to certain open account advances made by it as follows:

(i) $5,494,722.00 to the Debtor.
(ii) 856,260.00 to Sacramento Northern Railway Company.
(iii) 120,000.00 to Standard Realty and Development Company.

(c) Debtor's equity in collateral theretofore and thereafter deposited by it with Reconstruction Finance Corporation.

(d) [1]Debtor's right to distributive shares in the fund administered by The Railroad Credit Corporation under the Marshalling and Distributing Plan, 1931.

(e) [1]Assignment of distributive shares of Deep Creek Railroad Company, Sacramento Northern Railway.

The principal amount of each of R. C. C.'s loans has been reduced from time to time by income from collateral, including application of distributive shares, by way of credits, so that as of the effective date of the Plan, to wit, January 1, 1939, the unpaid balance of principal was $2,445,609.88. Added to this amount the accrued and unpaid interest to the effective date of the Plan of $145,314.25, makes a total claim of $2,590,924.11 (R. 1576).

2. The Reconstruction Finance Corporation:

The claim of the Reconstruction Finance Corporation (hereinafter referred to as Finance Corporation or R. F. C.) is evidenced by five notes representing loans to the Debtor Company in the principal sum of $2,963,000, plus accrued

[1] The net contributions originally made to the Marshalling and Distributing Fund by the Debtor, the Deep Creek and Sacramento Northern Railway Companies, and subsequently pledged or authorized to be applied against the loan obligations of the Debtor, amounted to $200,705.30. As of January 1, 1939, the effective date recommended for the Plan, there had been distributed 77½% of this sum, leaving a net contributed balance of $45,158.66, plus allocated income from the aforementioned Fund amounting to $9,897.70, which, added together, left an undistributed book balance of $55,056.36.

interest to the effective date of the Plan in the amount of $899,869.98, or a total note claim of $3,862,869.98 (R. 1576). These notes are secured by the following collateral: (R. 1577)

$8,750,000 of Debtor's General and Refunding Mortgage bonds, Series A, and

2,000,000 of the same refunding mortgage bonds, Series B,

Voting trust certificates for 150,000 shares of common stock of Denver & Rio Grande Western Railroad Company,

A second lien on $2,000,000 of refunding mortgage bonds, Series A, pledged with the R. C. C.

3. The A. C. James Company:

Debtor's loan obligation to the A. C. James Company (hereinafter referred to as the James Company) is evidenced by notes representing loans in the principal sum of $4,999,800, with accrued interest of $1,249,950 to effective date of the plan, or an aggregate total claim of $6,249,750. The following collateral secures the notes of this creditor: (R. 1577-78)

$6,249,500 principal amount of Debtor's General and Refunding Mortgage Bonds, Series A, of which $2,000,000 were repledged by the James Company with the R. C. C. and on which the R. C. C. has a prior lien.

The above represents all of the collaterally secured note claims filed in this proceeding and as security for which the total issue of Debtor's First and General Mortgage Bonds in the aggregate amount of $18,999,500 has been pledged. Each of these loans was, of course, made to the Debtor *prior* to the bankruptcy proceedings, and in the case of the R. F. C. and the A. C. James Company with the approval of the Commission.

Quite distinct from these three loans made to the debtor before the bankruptcy petition is the loan made by the R. F. C. to the Trustees *after the bankruptcy petition*. This latter loan (R. 696), evidenced by $10,000,000 of Trustees Certificates authorized by the Court, is a first lien on the estate prior to all other liens except taxes and is *pari passu* with other expenses of administration.

Turning now to the plan of reorganization approved by the District Court, the treatment with respect to the allocation of new securities for each of these claims as recommended therein is as follows:

> "O. The $10,000,000 of new first mortgage bonds, series A, to be authenticated and issued in the reorganization shall be sold at par and accrued interest to the Reconstruction Finance Corporation * * *. In consideration of such purchase by the Reconstruction Finance Corporation of the new first-mortgage bonds, series A, and considering the value of the collateral securing its claim, such claim amounting as of January 1, 1939, to $3,862,870 ($2,963,000 principal and $899,870 interest) and represented by notes secured by general and refunding bonds of the debtor and other collateral, shall be provided for under the plan in like securities and in like proportions as those given holders of the debtor's first mortgage bonds." (R. 389-90).
>
> "3. The Reconstruction Finance Corporation shall receive in respect of the $10,000,000 of new money provided for in subdivision O (or the surrender of trustees'-certificates at their principal amount and accrued interest, to a like amount) and its existing claim in the principal amount of $2,963,000, together with $899,870 of interest accrued and unpaid thereon to January 1, 1939, approximately $10,000,000 of new first-mortgage 4-percent bonds, series A (being 100 percent of said new money); $1,185,200 of income-mortgage 4½-percent bonds, series A (being 40 percent of the

principal of said claim); $1,777,800 of 5-percent preferred stock, series A (being 60 percent of the principal of said claim); and 15,788 shares of common stock (being common stock taken at the price of $57 a share for 100 percent of said accrued and unpaid interest). (R. 391).

"4. The Railroad Credit Corporation shall receive in respect of its claim in the principal amount of $2,455,610, together with $146,503 of interest accrued and unpaid thereon to January 1, 1939 (subject to the reduction of said amounts by the application, prior to the date of issue of new securities under the plan, of any proceeds from the distributive shares of the company or its subsidiaries under the marshaling and distributing plan, 1931), approximately $154,111 of income mortgage 4½-percent bonds, series A; $241,681 of 5-percent preferred stock, series A; and 35,425 shares of common stock (being common stock taken at the price of $62 per share). The Railroad Credit Corporation's equity in the collateral securing the claim of the Reconstruction Finance Corporation is found to be without value. (R. 391-92).

"5. The A. C. James Company shall receive in respect of its claim in the principal amount of $4,999,800, together with $1,249,950 of interest accrued and unpaid thereon to January 1, 1939, $163,724 of income mortgage 4½-percent bonds, series A; $256,756 of 5-percent preferred stock, series A; and 37,635 shares of common stock (being an amount of common stock which bears to the amount of common stock allotted to the claim of the Railroad Credit Corporation the same proportion that the principal amount of general and refunding mortgage bonds of the debtor held by the A. C. James Company as collateral for said claim, bears to the principal amount of such bonds held by the Railroad Credit Corporation as collateral for its claim). (R. 392)."

After commenting generally upon the value of the assets pledged under the General and Refunding Mortgage, the approved Plan of the Commission concludes that—

> "xxx the creditors secured by the general and refunding mortgage bonds should be awarded new income mortgage bonds in the amount of $732,010, and new participating preferred stock of a par value of $1,147,955. Applying to these amounts the proportionate amounts of general and refunding mortgage bonds securing the notes of the Finance Corporation, The Credit Corporation, and the James Company, the Finance Corporation would receive $414,175 of income mortgage bonds and $649,518 of new preferred stock, the Credit Corporation $154,111 of income-mortgage bonds and $241,681 of new preferred stock, and the James Company $163,724 of income bonds and $256,756 of new preferred stock for part of their claims. *However, this allocation will apply only to the Credit Corporation and the James Company, for, as appears herein, we approve the allocation of new securities to the Finance Corporation on a different basis, i.e., on the basis upon which securities are allotted to the holders of existing first-mortgage bonds.* In this connection we also find that such allocation of reorganization securities to the Finance Corporation exhausts the value of the collateral pledged by the debtor under the notes held by the Finance Corporation, and that the equity of the Credit Corporation in such collateral has no value." (R. 315–16). [Italics supplied]

The Commission therefore modified its prior report and order of October 10, 1938 (R. 194-299), which allocated as payment of the claims of the R. F. C., R. C. C. and James Company common stock of no-par-value for principal and interest, plus the right to subscribe within a fixed period of time for new first-mortgage bonds to be issued to provide new money (R. 294), and in its modification provided that the

Finance Corporation purchase the bonds at par and accrued interest and that in consideration of such purchase and the value of the collateral securing its claim, the Finance Corporation receive for the secured notes of the debtor held by it, treatment equal to that accorded the holders of the debtor's existing first-mortgage bonds. (R. 312).

It is quite apparent from the above extracts of the plan that the treatment in favor of R. F. C.'s note claim against the Debtor discriminates against the R. C. C. and the James Company, whose claims are similarly secured in part by general and refunding mortgage bonds. Since all three creditors are secured by these bonds (although in different amounts), they would be entitled to receive new securities in proportion to the respective amounts held, if it be assumed that the debtor's property and assets are insufficient in value to cover fully the claims of such creditors. But instead, the plan merges or consolidates R. F. C.'s distinct claim against the Debtor's Trustees for the loan of approximately $10,000,000 and secured by the Trustees' Certificates, with its separate note claim for $3,862,869.98 (R. 1576) against the Debtor Company, and then proceeds to treat both obligations as a single claim in order to accord to the R. F. C. treatment equal to that provided for the holders of Debtor's existing first mortgage bonds. By such action the plan thereby discriminates in favor of the R. F. C. and against the R. C. C. and the James Company. The Commission attempts to justify this preferred and discriminatory treatment on the ground that the raising of new money is necessary in order to secure funds to retire the $10,000,000 of Debtor's Trustees' Certificates held by the R. F. C., and states that the secured notes held by Reconstruction Finance Corporation are advanced to a preferred position and are entitled to receive treatment equal to that

given to First Mortgage bonds, in consideration of the purchase by that Corporation of the new $10,000,000 of first mortgage bonds at par and accrued interest (or the exchange of said certificates for the bonds) and in consideration of the value of the collateral securing the notes held by Reconstruction Finance Corporation. Thus, Reconstruction Finance Corporation would receive in respect of its secured note claim payment or refunding in new securities upon a basis equal to that accorded to First Mortgage bondholders.

Therefore, it is difficult to understand upon what hypothesis the plan attributes great value to the additional collateral pledged for the note claim of the R. F. C. Aside from the general and refunding mortgage bonds (including its second lien on $2,000,000 of the $4,000,000 of said bonds pledged with the R. C. C.) securing its claim against the Debtor, the only additional collateral which R. F. C. holds is 150,000 shares of common stock of the Denver & Rio Grande Western Railroad Company. This Court will take judicial notice of the fact that the Denver Company is presently reorganizing under Section 77 and that in its recent Supplemental Report and Order on a plan of reorganization the Commission found the stock to be of no value. (Finance Docket 11,002, July 13, 1942). In the face of this situation it is not easy to understand how the Commission can justify the following conclusion and treatment of R. F. C.'s note claim against the Debtor:

> "We will modify our prior report and order accordingly, and will also provide that the Finance Corporation purchase the bonds at par and accrued interest and that in consideration of such purchase *and the value of the collateral securing its claim*, the Finance Corporation receive for the secured notes of the debtor held by it, treatment equal to that accorded the holders of the

debtor's existing first-mortgage bonds." (R. 312). [Italics supplied]

Here are two separate and distinct loan obligations, one owed by the Debtor, the other by the Trustees of the Debtor. It is not denied, but willingly conceded, that Trustees' Certificates do enjoy a priority of payment ahead of first mortgage bondholders and secured noteholders because they rank as expenses of administration and therefore, constitute, equally with other expenses of administration, a direct charge and lien on all property of the Debtor held by the Trustees. The Credit Corporation does not dispute the soundness of this principle. On the contrary, it agrees that the Finance Corporation is entitled to cash for the Trustees' certificates or, failing in this, to the best security available to assure it of payment in full of its claim. The R. C. C. does object, however, to the consolidation or merger of the two claims and their treatment as a single unit of obligation in order that one of the claims may be advanced and receive preferred treatment in new securities which it otherwise would not get. General and refunding bonds are of no different value in the hands of the R. F. C. than they are in the hands of R. C. C. or of the A. C. James Company. The R. C. C. is pledgee of the equity in the collateral pledged with the R. F. C. including the $10,750,000 of Debtors General and Refunding Mortgage Bonds. The A. C. James Company holds a first lien on the equity in $2,000,000 of said bonds which it loaned to the Debtor to be pledged with the R. C. C. Were the plan to allocate new securities to these three claimants in an amount proportional to the amount of refunding bonds held by each as against the total of refunding mortgage bonds outstanding (not considering for this purpose the additional collateral securities) the fair and equitable distribution of new securities would be as follows:

The total General and Refunding Mortgage Bonds pledged is the entire issue of $18,999,500. Of these $10,750,000 have been pledged with the R. F. C., $4,000,000 with the R. C. C. and $4,249,500 with the A. C. James Company. Obviously then the proper distribution under the Commission's assumption would be represented in each case by a fraction whose denominator is $18,999,500 and whose numerator is the amount pledged to secure each claim.

The allotted securities for these claims total the following, $1,503,035, 4½% Income Mortgage Bonds, $2,276,237 5% Preferred Stock, 88,848 shares of Common Stock. This distribution applied to allotted securities results in the amounts shown below:

Creditors	4½% *Income Mtg. Bonds*	5% *Preferred Stock*	*Common Stock*
R. F. C. (.5638044)	$850,423.82	$1,287,904.91	50,270.59 shares
R. C. C. (.2105318)	316,436.66	479,220.27	18,705.33 shares
A. C. J. (.2236638)	336,174.52	509,111.82	19,872.08 shares
	$1,503,035.00	$2,276,237.00	88,848 shares

The above distribution assumes, though respondents deny, that the new securities represent the value of the general and refunding mortgage bonds which would be surrendered. Upon this assumption the allocation would be consistent with the principles enunciated by this Court in the [1]*Los Angeles Lumber Products Company* and the [2]*Rock Products Company* cases and should be substituted for the following distributions proposed by the Commission and approved by the District Court:

[1] Case v. Los Angeles Lumber Products Co., 308 U. S. 106.
[2] Consolidated Rock Products Co. v. DuBois, 312 U. S. 510.

Creditors	4½% Income Mtg. Bonds	5% Preferred Stock	Common Stock
R. F. C.	$1,185,200.00	$1,777,800.00	15,788 shares
R. C. C.	154,111.00	241,681.00	35,425 shares
A. C. J.	163,724.00	256,756.00	37,635 shares
	$1,503,035.00	$2,276,237.00	88,848 shares

Additional securities for the remainder of the rights which the R. C. C. now holds would, of course, also be necessary in order to retain its relative secured position in the reorganized company. It cannot be compelled to subordinate its rights in favor of a similarly secured noteholder simply because that claimant will purchase first mortgage bonds under the reorganization plan. The securities to be issued to the R. F. C. for any money to be furnished by it should be in recognition of the priority inherent in that transaction and not in any wise be connected with the treatment covering the loan by it to the Debtor as distinguished from the loan made by it to the Trustees.

In their briefs filed in this Court the R. F. C. and the Institutional Bondholders Committee have sought to justify the favored treatment for the R. F. C.'s claim on the ground among others, that the new first mortgage bonds, upon reorganization of the property, would sell for considerably less than par. This, now, is obviously absurd in view of the Trustees' petition to pay off a substantial portion from its cash on hand and on deposit with the R. F. C. (See Appendix A). Any way, this consideration is not only irrelevant to the grievance of the R. C. C., but offers no justification or support for treatment of another claim entirely foreign and distinct and which by no stretch of the imagination can be considered a part of the R. F. C.'s claim against the Trustees. There are no special equities applicable to the note claim of the R. F. C. which are not at least equally applicable to the claim of the R. C. C. The fact that the R. F. C. makes loans from

public moneys does not entitle it to special consideration. That the R. F. C., like other corporations, is subject to the general laws was so declared by this Court in the [1]*Rock Island* case, wherein this Court said:

> "The Reconstruction Finance Corporation Act creates a corporation and vests it with designated powers. Its entire stock is subscribed by the government, but it is none the less a corporation, limited by its charter and by the general law. The act does not give it greater rights as to the enforcement of its outstanding credits than are enjoyed by other persons or corporations in the event of proceedings under the Bankruptcy Act. The provisions and principles of enforcement of the Bankruptcy Act, including Section 77, are binding upon the Reconstruction Finance Corporation, in the absence of some pertinent statutory exception, as they are upon other corporations."

Unlike the ordinary proceeding in bankruptcy where the assets of the bankrupt are converted into cash for distribution among his creditors, Section 77 "is a special proceeding which seeks only to bring about a reorganization, if a satisfactory plan to that end can be devised." [1]*Rock Island* case, *supra*. A plan which singles out a claim secured by the same character of bonds as those of other creditors and applies to it treatment *pari passu* with the claims of mortgage bondholders simply because of its willingness to exchange a separate claim against the Debtor Trustees is obviously unfair and *in*equitable. This is the more apparent because the claim against the Trustees based on their certificates is a first lien against the estate, ranking *pari passu* with expenses of administration.

The record shows that on orders of the District Court the Trustees' certificates have been refunded from time to time

[1] Continental Illinois National Bank & Trust Co. v. Chicago, Rock Island & Pacific Railway Co., 294 U. S. 648, 684.

by an extension of their respective maturity dates and by the issue of new certificates of indebtedness of equal principal amount. Petitioners refer (R.F.C.'s brief, page 41) to the opinion of the District Court denying this motion to use $3,000,000 of the Trustees' cash to retire an equal amount of Trustees Certificates, and in the Institutional Bondholders brief, (pages 110 and 111), this language occurs

> "The rapidly mounting gross income of the Debtor's properties, before Federal taxes, is resulting in a rapid accumulation of cash by the reorganization trustees. As of September 1, 1942, the cash on hand and on deposit with R. F. C. aggregated $10,493,000, of which a substantial amount, however, must be reserved for taxes and deferred maintenance, as well as for the additions and betterments necessary to meet additional traffic demands. If any of the remaining cash is used to pay down, or possibly pay off, the Trustees' Certificates, so that the R. F. C. Notes will be left to be dealt with solely upon the basis of their pledged Refunding Bonds, the reorganized company will be denuded of the cash necessary to service the new securities from January 1, 1939, the effective date of the Commission Plan. Not only will the First Mortgage Bondholders' realization of any cash income out of the earnings of their properties thus be substantially delayed to their own injury, but if the Commission Plan is thus rendered abortive, at least $10,000,000 more of interest will have accrued upon the First Mortgage since January 1, 1939. This will have to be provided for in any new plan with due recognition of its priority over the pledged Refunding Bonds."

Both the R. F. C. and the Institutional Bondholders Counsel overlooked or failed to comprehend the language of the latest petition duly served on the parties hereto and filed with the District Court under date of September 4, 1942, a petition brought by the Trustees on their own motion and verified by Charles Elsey, the President of the Western Pacific Railroad

Company, and since the appointment of the Trustees of the properties of said company, the agent of said trustees in immediate charge of the railroad and other property of said Company. Said petition is annexed to this brief as Appendix A. The following significant extracts appear in the petition:

"Your petitioners also put up with the Reconstruction Finance Corporation, incidentally to said further extension of said loan to December 1, 1942, and as collateral security therefor, the sum of $5,000,000 from cash in the hands of your petitioners, pursuant to said order. On April 24, 1942, your petitioners put up with Reconstruction Finance Corporation, as further collateral security for said loan and subject to the same terms and conditions, the additional sum of $1,000,000 from cash in the hands of your petitioners. Pursuant to said order of November 26, 1941, and said agreement by your petitioners with the Reconstruction Finance Corporation, your petitioners have curtailed the principal of said loan by the amount of $25,000 on the 15th day of the months of December, 1941, to August, 1942, both inclusive, thereby reducing the said principal of said loan to the total amount of $9,625,000, and the said Certificates of Indebtedness in said reduced principal amount are now outstanding and held by Reconstruction Finance Corporation and mature and are payable on December 1, 1942. Your petitioners have paid to Reconstruction Finance Corporation the interest upon the said outstanding Certificates of Indebtedness to and including the 1st day of September, 1942. Your petitioners will further curtail the principal of said loan by the amount of $25,000 on the 15th day of each of the months of September, October and November, 1942, thereby reducing the said principal of said loan to the total amount of $9,550,000.

* * * *

"Your petitioners had cash on hand as of September 1, 1942, in the total amount of $4,493,000 and they expect to have cash on hand as of December 1, 1942, after meeting all expenses to be incurred in the opera-

tion and maintenance of the properties of the Debtor, in the total amount of not less than $6,000,000. In addition thereto, as hereinbefore set forth, your petitioners have put up with the Reconstruction Finance Corporation the total amount of $6,000,000 incidentally to and as collateral security for said further extension of said loan. Petitioners are of the opinoin that they would be able, without impairment of necessary working capital and without prejudice to the conduct of the railroad business of the Debtor, to retire by redemption out of cash on hand and said cash put up with the Reconstruction Finance Corporation a substantial portion of the principal amount of the indebtedness represented by said outstanding certificates of indebtedness. By reason of said increase in the amount of cash available to your petitioners, including said sums put up with and now held by the Reconstruction Finance Corporation, and said order of this Court made on May 13, 1941, your petitioners desire to receive instructions from this Court with respect to the partial retirement of said indebtedness and, if such partial retirement should be ordered by the Court, the amount thereof."

Pursuant to Order of the Court issued under date of September 4, 1942, hearing on said petition was ordered for September 28, 1942.

The argument presented in these briefs of petitioners seems to carry its own refutation. The money borrowed from the R. F. C. by the Trustees (not the Debtor) under the order of the court constitutes a debt which should be discharged before reorganization if the cash is available with which to discharge it. It is prior to all other claims excepting taxes. It is of equal rank with administration expenses. To say that payment should be deferred because the First Mortgage Bondholders might be delayed in receiving payment on their bonds is to give to those First Mortgage Bondholders the priority and preference which belongs to the Trustees' Certificates. The

statement of the Trustees that they can pay a substantial portion of the debt; that they have $6,000,000 of cash deposited with the R. F. C. and expect to have six million more on hand on December first, at which time they can, without impairing in anywise the reorganization, pay off a substantial portion of the Trustees' Certificates, would seem to be more persuasive than the opinion of counsel for First Mortgage Bondholders that because of such payment the reorganized company will be denuded of the cash necessary for deferred maintenance [of which there is none in evidence] as well as for additions and betterments necessary to meet additional traffic demands and to service the new securities issued to the First Mortgage Bondholders. The responsibility for the future operation of this property is upon these Trustees and upon Mr. Elsey, the President, who has sworn to the statements contained in the petition. These should have a greater probative value than the argument of petitioners counsel in their briefs.

If these certificates are paid off before or at the time of the consummation of a plan which accords to the R. F. C. treatment similar to that now recommended in the Commission's plan, the unfairness of this arrangement becomes increasingly apparent. The remaining note claim of the R. F. C. in this event would then enjoy a larger amount of new securities which it obtained in consideration of its acceptance of $10,000,000 of new first mortgage bonds for the surrender of the said certificates of indebtedness instead of insisting upon cash. In other words, it now seems probable that these certificates will be paid in full before consummation of any plan. In this event the consideration which prompted preferential treatment of R. F. C.'s note claim will disappear. Assume, on the other hand, that the certificates are not paid in cash before consummation of a plan which accords similar treatment to R. F. C., then this claim against the Trustees

will have been paid by the allocation of $10,000,000 of new first mortgage bonds. It is a reasonable prediction, that the principal amount of the certificates will be appreciably less than the $10,000,000 of first mortgage bonds because of the current retirements and the allegations in the petition of the Trustees for authority to pay a "substantial portion of the principal amount of the indebtedness represented by said outstanding certificates of indebtedness."

It is the contention of the Credit Corporation that inasmuch as the three noteholders all hold similar collateral, *i.e.*, general and refunding mortgage bonds, their claim should be refunded, under the Commission's assumption, so far as this collateral is concerned, in new securities of the same grades in proportion to the respective amounts of collateral held by each such noteholder. "Rights of several parties similarly circumstanced should all stand on the same footing." *In re Mortgage Guarantee Co.*, C. C. H. 53,093 (not officially reported in Federal Supplement). Therefore, the claims of the Credit Corporation and the James Company, to the extent that they are secured by similar bonds, or equivalent value, are entitled to comparable treatment, but the Plan does not so provide. Participation in the reorganization by all claimants should be, as the Court below has found, "in proportion to the value of their respective claims." (R. 2669). The effect of the consideration imputed to R. F. C.'s note claim but not valued by the Commission or the District Court, is to place it in the category of an obligation adequately secured and ranking equally with first mortgage bonds upon a basis which discriminates unfairly against R. C. C. and A. C. James Company. In the absence of such a determination the plan fails to meet the purposes of Section 77, which "include the development of a 'fair and equitable' plan of reorganization." [1] *Warren, et al., Trustees vs. Palmer, et al., Trustees.*

[1] Warren, et al., Trustees v. Palmer, et al., Trustees, 310 U. S. 132, 140.

It is respectfully submitted that the securities to be issued to the R. F. C. for any money to be furnished by it, or as an exchange for any securities to be surrendered, should be in recognition of the priority inherent in that transaction and not in any wise connected with the treatment covering the loan by the Reconstruction Finance Corporation to the Debtor as distinguished from the loan made by R. F. C. to the Trustees.

POINT TWO

The limitation on capitalization fixed in the Plan approved by the District Court does not constitute a valuation or appraisal of the Debtor's property including the actual investment therein, such as is required by Section 77 of the Bankruptcy Act, as Amended and the law of the land.

Section 77(e) contains the following provision requiring a valuation of the debtor's properties if a valuation shall be necessary for any purpose:

> "If it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts."

Section 77(b) also requires that the plan of reorganization

> "* * * (4) shall provide for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent

for leased railroads) in such an amount that, after due consideration of the probable prospective earnings of the property in light of its earnings experience and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof; * * * ."

Are additional powers conferred, or additional duties imposed upon the Commission by the above quoted clauses of Section 77?

An accurate or even illuminating answer to this question involves an examination of the "law of the land" at the date of the enactment of Section 77 and a recital of legislative and judicial action up to that date.

Valuation and capitalization of railroads by the Interstate Commerce Commission were originally urged by the Commission in its report to Congress in 1908 in the following language:

> "A second consideration which leads the Commission to urge upon Congress provision for an authoritative valuation of railway property is the importance which the question of capitalization has assumed in recent years. No one at the present time can say whether railways are undercapitalized or overcapitalized; or, should objection be made to that way of putting the question, no one can say, with the information in hand, which of the roads are undercapitalized and which are overcapitalized. A valuation adequate to the problem in hand should not stop with the simple statement of an amount; on the contrary it should analyze the amount ascertained according to the sources from which the value accrues and show the economic character as well as the industrial significance of the several forms of value. In no other way is it possible to arrive at an intelligent understanding of that complex situation suggested by the phrase 'railway capitalization'."
>
> "A third argument in support of the plan of an authoritative valuation of railway property is found in the present unsatisfactory condition of railway balance

sheets. The balance sheet is, perhaps, the most important of the statements that may be drawn from the accounts of corporations, for, if correctly drawn, it contains not only a classified statement of corporate assets and corporate liabilities, but it provides in the balance, that is to say, the 'profit and loss' a quick and trustworthy measure of the success that has attended the operation and management of the property. Every balance sheet begins with 'cost of property' against which is set a figure which purports to stand for the investment. This is no place to enter upon an extended criticism of the practice of American railways in the matter of their property accounts, nor is such a criticism necessary for the purpose in hand. It is sufficient to refer to the well known fact that no court, or commission, or accountant, or financial writer would for a moment consider that the present balance sheet statement purporting to give the 'cost of property' suggests, even in a remote degree, a reliable measure either of money invested or of present value. Thus, at the first touch of critical analysis, the balance sheets published by American railways are found to be inadequate. They are incapable of rendering the service which may rightly be demanded of them. One cure seems possible for such a situation, and one only, and that is for the Government to make an authoritative valuation of railway property, and to provide that the amounts so determined should be entered upon the books of the carriers as the accepted measure of capital assets. Under no other condition can the Commission complete in a satisfactory manner the formulation of a standard system of accounts." Twenty-Second Annual Report of the Interstate Commerce Commission, 1908, pp. 84, 85.

It is significant that the above quotation was no temporary unconsidered conclusion of the Commission, for it used the same language in its annual reports to Congress in 1910 and 1911 and re-affirmed in each case its conclusions.

Twenty-Fourth Annual Report of the Interstate Commerce Commission, 1910, p. 37.

Twenty-Fifth Annual Report of the Interstate Commerce Commission, 1911, pp. 93, 94.

Valuation Act, 1913, Section 19a

On March 1, 1913, Congress enacted what is generally referred to as Section 19a of the Interstate Commerce Act (49 U. S. C. A., p. 64). In Section 19a Congress directed the Interstate Commerce Commission to make a physical valuation of the property of common carriers subject to the provisions of the Interstate Commerce Act. This valuation should begin with an inventory which shall "list the property of every common carrier subject to the provisions of this chapter in detail, and show the value thereof as hereinafter provided, and shall classify the physical property, as nearly as practicable, in conformity with the classification of expenditures for road and equipment, as prescribed by the Interstate Commerce Commission."

In determining the physical valuation of property, the Commission was required to "ascertain and report in detail as to each piece of property, other than land, owned or used by said common carrier for its purposes as a common carrier, the original cost to date, the cost of reproduction new, the cost of reproduction less depreciation, and an analysis of the methods by which these several costs are obtained, and the reason for their differences, if any." The Commission was required in like manner to "ascertain and report separately other values, and elements of value, if any, of the property of such common carrier, and an analysis of the methods of valuation employed, and of the reasons for any differences between any such value and each of the foregoing cost values."

"Second. Such investigation and report shall state in detail and separately from improvements the original cost of all lands, rights of way, and terminals owned or used for the purpose of a common carrier, and ascertained as of the time of dedication to public use, and the present value of the same."

"Third. Such investigation and report shall show separately the property held for purposes other than those of a common carrier, and the original cost and present value of the same, together with an analysis of the methods of valuation employed."

The Commission was further directed to investigate and report upon the history and organization of "the present and of any previous corporation operating such property". The Commission was also required to "ascertain and report the amount and value of any aid, gift, grant of right of way, or donation, made to any such common carrier." The Commission was required as a result of such investigation to show "the value of the property of every common carrier as a whole and separately the value of its property in each of the several States and Territories and the District of Columbia, classified and in detail as herein required."

The Act goes on to require the Commission upon the completion of the valuation to "keep itself informed of all extensions and improvements or other changes in the condition and value of the property of all common carriers, and shall ascertain the value thereof, and shall from time to time, revise and correct its valuations, showing such revision and correction classified and as a whole and separately in each of the several States and Territories and the District of Columbia, which valuations, both original and corrected, shall be tentative valuations and shall be reported to Congress at the beginning of each regular session. (g) To enable the Commission to make such changes and corrections in its valuations of each

class of property, every common carrier subject to the provisions of this chapter shall make such reports and furnish such information as the Commission may require. * * * "

"All final valuations by the Commission and the classification thereof shall be published and shall be prima facie evidence of the value of the property in all proceedings under this chapter as of the date of the fixing thereof, and in all judicial proceedings for the enforcement of this chapter, and in all judicial proceedings brought to enjoin, set aside, annul, or suspend, in whole or in part, any order of the Interstate Commerce Commission."

"(j) If upon the trial of any action involving a final value fixed by the Commission, evidence shall be introduced regarding such value which is found by the court to be different from that offered upon the hearing before the Commission or additional thereto and substantially affecting said value, the court, before proceeding to render judgment shall transmit a copy of such evidence to the Commission, and shall stay further proceedings in said action for such time as the court shall determine from the date of such transmission. Upon the receipt of such evidence the Commission shall consider the same and may fix a final value different from the one fixed in the first instance, and may alter, modify, amend or rescind any order which it has made involving said final value, and shall report its action thereon to said court within the time fixed by the court. If the commission shall alter, modify, or amend its order, such altered, modified, or amended order shall take the place of the original order complained of and judgment shall be rendered thereon as though made by the Commission in the first instance. If the original order shall not be rescinded or changed by the Commission, judgment shall be rendered upon such original order."

This last citation of paragraph (j) is to bring out the fact that under Section 19a the final valuation found by the

Commission was only prima facie evidence of value; that the actual determination of a final value was a judicial act involving the rendition of judgment upon the findings of the Commission and the evidence introduced at the trial of any action involving a final value fixed by the Commission.

Transportation Act, 1920, Section 15a

On February 28, 1920, Congress enacted the Transportation Act of that date. The following are pertinent quotations from Section 15a of that Act (49 U. S. C. A., p. 443):

"(2) *Rates to permit carriers to earn fair return.* In the exercise of its power to prescribe just and reasonable rates the commission shall initiate, modify, establish or adjust such rates so that carriers as a whole (or as a whole in each of such rate groups or territories as the Commission may from time to time designate) will, under honest, efficient and economical management and reasonable expenditures for maintenance of way, structures and equipment, earn an aggregate annual net railway operating income equal, as nearly as may be, to a fair return upon the aggregate value of the railway property of such carriers held for and used in the service of transportation: *Provided,* That the commission shall have reasonable latitude to modify or adjust any particular rate which it may find to be unjust or unreasonable; and to prescribe different rates for different portions of the country.

"(3) *Determination of percentage constituting fair return.* The commission shall from time to time determine and make public what percentage of such aggregate property value constitutes a fair return thereon, and such percentage shall be uniform for all rate groups or territories which may be designated by the commission. In making such determination it shall give due consideration, among other things, to the transportation needs of the country and the necessity (under honest, efficient and economical management of existing transportation facilities) of enlarging such facilities in order

to provide the people of the United States with adequate transportation.

"(4) *Determination of aggregate value of properties.* For the purposes of this section, such aggregate value of the property of the carriers shall be determined by the commission from time to time and as often as may be necessary. The commission may utilize the results of its investigation under Section 19a of this chapter, in so far as deemed by it available, and shall give due consideration to all the elements of value recognized by the law of the land for rate-making purposes, and shall give to the property investment account of the carriers only that consideration which under such law it is entitled to in establishing values for rate-making purposes. Whenever pursuant to Section 19a of this chapter the value of the railway property of any carrier held for and used in the service of transportation has been finally ascertained, the value so ascertained shall be deemed by the commission to be the value thereof for the purpose of determining such aggregate value."

This was the "law of the land" as such law had been enacted by Congress at the time of the passage of the enactment of Section 77. Added to that is the constitutional protection of the Fifth Amendment and the decisions of this court in the series of cases beginning with the [1]*Minnesota Rate Cases.*

That it was then the "law of the land" was clearly set forth by the Chief Justice in the unanimous opinion of this Court in the case of [2]*Dayton-Goose Creek Railway Company Case* (decided January 7, 1924) and specifically in the following language on page 478:

Referring to the Transportation Act of 1920, the opinion says:

"The new act seeks affirmatively to build up a system of railways prepared to handle promptly all the interstate traffic of the country. It aims to give the owners

[1] Minnesota Rate Cases, 230 U. S. 352.
[2] Dayton-Goose Creek Railway Company v. United States, 263 U. S. 456.

of the railways an opportunity to earn enough to maintain their properties and equipment in such a state of efficiency that they can carry well this burden. To achieve this great purpose, it puts the railroad systems of the country more completely than ever under the fostering guardianship and control of the Commission, which is to supervise their issue of securities, their car supply and distribution, their joint use of terminals, their construction of new lines, their abandonment of old lines, and by a proper division of joint rates, and by fixing adequate rates for interstate commerce, and, in case of discrimination, for intrastate commerce, to secure a fair return upon the properties of the carriers engaged."

* * *

"To regulate in the sense intended is to foster, protect, and control the commerce with appropriate regard to the welfare of those who are immediately concerned, as well as the public at large, and to promote its growth and insure its safety."

Previously this Court on February 19, 1923, had in a unanimous opinion, written by Mr. Justice Brandeis, expressed a similar view of the "law of the land" in the following language:

"Transportation Act, 1920, introduced into the Federal legislation a new railroad policy. *Railroad Commission v. Chicago, B. & Q. R. R. Co.*, 257 U. S. 563, 585, 66 L. ed. 371, 382, 22 A. L. R. 1086, 42 Sup. Ct. Rep. 232. Theretofore, the effort of Congress had been directed mainly to the prevention of abuses; particularly, those arising from excessive or discriminatory rates. The 1920 Act sought to insure, also, adequate transportation service. That such was its purpose, Congress did not leave to inference. The new purpose was expressed in unequivocal language. And to attain it, new rights, new obligations, new machinery, were created. The new provisions took in a wide range. Prominent among them are those specially designed to

secure a fair return on capital devoted to the transportation service. Upon the Commission new powers were conferred and new duties were imposed."

New England Divisions Cases, 261 U. S. 184, 189. See also *Railroad Commission v. Chicago B. & Q. R. R. Co.*, 257 U. S. 563.

These legislative enactments and the decisions of this Court warrant a presumption of a substantial and conclusive character that the valuation of a railroad ascertained and brought down to any given date pursuant to the provisions of Section 19a is the value upon which the owners of the railroad property are entitled to earn, if they can, a fair return, and that this value cannot be taken away from them excepting by judicial decree. The legislative department of this Government cannot, without judicial sanction, deprive such owners of the value so determined. It is true that in an equity proceeding a sale by foreclosure may eventually establish as the value the price which the property brings at such foreclosure sale, but this is not an equity receivership. This is a reorganization of a company not found to be insolvent under the provisions of the Bankruptcy Act. In the absence of such insolvency there is no warrant for saying that the value of such property upon reorganization, as is necessary or appropriate for the efficient and economical performance of transportation, shall be other than the valuation found under Section 19a and brought down to date by the Commission. If there be any part of the bankrupt estate which the Commission in approving the plan finds to be of not sufficient use to warrant its inclusion in the reorganized estate, it is the Commission's duty so to express itself and to exclude the same from the value placed upon the remaining property. In this case the Commission has made no such finding but has expressly found that the property is not now under-maintained. From this it follows that the entire

property has been found to be used or useful for performing the work of an economical and efficient transportation agency.

What then does Section 77(e) mean by the clause "if it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new, less depreciation, and original cost of the property and the actual investment therein as may be required under the law of the land in the light of its earning power and all other relevant facts."

The "probable prospective earnings" of the property should be the guide to the Commission in performing the duty imposed upon it not by (e), under which the standard is earning power, but by (b) of Section 77 which, as above quoted, requires that the plan of reorganization

> "* * * (4) shall provide for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such an amount that, after due consideration of the probable prospective earnings of the property in light of its earnings experience and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof; * * *."

This subsection places upon the Interstate Commerce Commission the responsibility in fixing the capitalization of the reorganized company to provide for the issue of obligations which the reorganization carrier may assume, carry and eventually pay, while continuing to function as a solvent and

prosperous carrier capable of providing for the maximum transportation needs of the territory which it serves. This providing should include funds necessary for maintaining the carrier's facilities, so that under honest, efficient and economical management it will in the future be able to furnish adequate transportation. This is substantially the language of paragraph (3) of Section 15a and sets forth a duty which is clearly within the legislative powers conferred upon the Interstate Commerce Commission. Indeed, it is the standard outlined or expressed by this court in the *New England Divisions Cases* and the *Dayton-Goose Creek Case*, above cited, and it is entirely consistent with the authority given to the Interstate Commerce Commission under Section 20a, (49 U. S. C. A., p. 290), wherein the Commission is authorized to make an order with respect to the issuance of securities and the assumption of obligations only if such issuance or assumption "is for some lawful object within its corporate purposes, and compatible with the public interest, which is necessary or appropriate for or consistent with the proper performance by the carrier of service to the public as a common carrier, and which will not impair its ability to perform that service, and (b) is reasonably necessary and appropriate for such purpose." From this may be deduced the conclusion that the duty of the Interstate Commerce Commission in fixing capitalization for a reorganized corporation is principally to determine what obligations the reorganized corporation should assume, the principal amount and character of those which involve fixed interest payments, and the total amount and character of contingent obligations, only to the extent in the latter case of prescribing principal amounts and maturities which the reorganized corporation will meet and will be able to discharge upon maturity. These obligations are the test of what the reorganized carrier must do in order to function efficiently and economically as a reor-

ganized corporation without danger of being forced again into another reorganization. When these amounts have been determined and have been assigned to claimants in the order of priority, the remaining value of the property should in accordance with the doctrine of [1]*Northern Pacific Railway v. Boyd*, [2]*Case v. Los Angeles Lumber Products Co., Ltd.*, [3]*Consolidated Rock Products Co. v. Du Bois*, be allotted to junior creditors whose claims have not been satisfied and whatever equity is left to the remaining stockholders.

It is this remaining value which is beyond the administrative power of the Commission to tamper with. True, it may as a sort of statutory special master, advise the District Court upon valuation or any other relevant fact and this advice when based upon adequate evidence or proof received at a hearing is entitled to weight. But the Commission cannot by its mere fiat condemn a solvent carrier to insolvency solely because under the provisions of Section 77 the carrier has sought the protection of the Court alleging its temporary inability to pay its debts as they mature. Before such condemnation there must be a hearing and a finding that the capital assets are not, at a fair valuation, sufficient in amount to pay the debts (Bankruptcy Act, Section 1, (19)). This is the valuation which the Commission definitely has failed to find in the current case. This is the valuation necessary to be found by the Commission in obedience to the mandate of Congress expressed in paragraph (e) of Section 77. For this failure the Commission should be dealt with by this Court as it was dealt with for a similar disobedience in [4]*St. Louis & O'Fallon Railway Co. v. United States*, at which latter page the following language is quoted from this opinion:

> "In the exercise of its proper function this Court has declared the law of the land concerning valuations for rate-making purposes. The Commission disregarded

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[1] Northern Pacific Railway v. Boyd, 228 U. S. 482.
[2] Case v. Los Angeles Lumber Products Co., Ltd., 308 U. S. 106.
[3] Consolidated Rock Products Co. v. Du Bois, 312 U. S. 510.
[4] St. Louis & O'Fallon Railway Co. v. United States, 279 U. S. 461, 487.

the approved rule and has thereby failed to discharge the definite duty imposed by Congress. Unfortunately, proper heed was denied the timely admonition of the minority: 'The function of this commission is not to act as an arbiter in economics, but as an agency of Congress, to apply the law of the land to facts developed of record in matters committed by Congress to our jurisdiction'. * * * Whether the Commission acted as directed by Congress was the fundamental question presented. If it did not, the action taken, being beyond the authority granted, was invalid."

The proposed reorganization plan would, if carried out, inflict an unwarranted injustice upon the stockholders of the Debtor to whom it would deny any equity in a property to which on October 10, 1938, the Commission gave a valuation in the following words (R., p. 224):

> "If there be added to the above amounts the net costs of additions and retirements between valuation dates and December 31, 1935, the total would be $139,600,455."

The proposed reorganization plan would fix the capitalization at $97,763,522, treating the no-par-value common stock at $100 per share (R., p. 364). Even under this figure the secured claims against the Debtor in the total amount of $87,922,143 (which includes $10,000,000 of Trustees' Certificates) should be refunded in full, leaving a balance of approximately $10,000,000 for the unsecured debt and the stockholders' interests. In fact, however, the Commission has cut-off entirely the capital stock of the Debtor and the unsecured claims against the Debtor; and, in addition, the Commission has scaled down the secured claims. Aside from the unfair treatment of the stockholders and creditors, however, it should be noted that the capitalization recommended by the Commission would deny any equity to the difference between the above valuation of $139,-

600,455 and the capitalization permitted of $97,763,522 or $41,836,933; would bar unsecured creditors from any realization upon their claims and forever deprive the stockholders who have invested their money in this corporation from any voice in the reorganized corporation and from any chance to recoup their losses. It is submitted that the conclusion of the Commission is without warrant when it says (R., p. 257) "that based on the most optimistic estimate of earnings of record, the capitalization of the reorganized company must be maintained within strict limits if any material return on its capital stock is to be expected and the shares of its stock are not to become mere tokens for stock market speculation." Herein the Commission would seem to abdicate the control over the issuance of securities and obligations as given to it under Section 20a and assume a defeatist attitude which the value of the property and its current earnings do not warrant. If stockholders making honest and conservative investments were permanently disfranchised because of no dividends during years of depression, then most of the railroads of the United States during the twelve years from 1928 to 1940 would have been without stockholder management.

"The value of a railroad for capitalization purposes should therefore not be based on what it has earned in the past under regulatory restrictions, nor what it might be expected to earn in the future under regulatory restrictions. It should be based on some formula involving a physical valuation of assets used and useful in the public service. Pessimistic forecasts, or even optimistic forecasts, as to what these assets may be expected to earn in the indefinite future have no place in determining capitalizable value. A capitalization that represents prudent investment is based on firm ground. Such a capitalization accurately represents the property on which the railroad should be permitted to

earn a fair return if, under competitive conditions, it can do so. Forecasts as to the chances of its succeeding are not only largely guesswork, but are wholly unnecessary and should be eliminated from the problem, especially when these forecasts are definitely final and extend without limitation in time. Forecasts of a few years ahead, or even months, are often unreliable. Forecasts of the future earnings of a road as a whole with no limit of time, to be used as a base for a recapitalization which permanently wipes out investors are an absurdity." [F. R. Dick, *Railway Age*, September, 1942, p. 489].

Since 1920 the stockholders of the railroads of the United States have made their investments in the properties of those railroads, relying upon the assurance contained in the Transportation Act of 1920 that the Interstate Commerce Commission would so regulate the revenues that they would be entitled, if at all possible, to earn upon the property used or useful in transportation a fair return upon the value of such property. During that period the Interstate Commerce Commission has not only regulated such revenues and practically fixed them, but it has to a very considerable extent regulated the cost of producing such transportation. In these circumstances, good faith requires that the stockholders' share in the value of the property fixed by the Commission under Section 19a should be protected. Unless and until such property or any portion thereof is found to be neither used nor useful for the purpose for which the railroad was created, these stockholders are entitled to the fostering care of the Commission. Only to the extent that any portion of such property has ceased to be used or useful for transportation may its value be written off the balance sheet of the transportation agency. To say that value should now be related to the ability of the railroads to pay dividends during depression periods is an attempt to deprive these stockholders of their property without due process of law.

Conclusion

It is respectfully submitted that the decree of the Court below was proper, and that the plan of reorganization as approved by the District Court was unfair and inequitable and failed to meet the requirements contemplated by Section 77 as to the valuation of the Debtor's property and a proper allocation of new securities based upon the value of the several claims, and more especially the discriminatory treatment of the note claim of the Reconstruction Finance Corporation at the expense of the claims of The Railroad Credit Corporation and the A. C. James Company. Therefore, said decree of the Court below should be affirmed and the proceeding referred back to the Interstate Commerce Commission for further action and a determination of the value of Debtor's assets and properties in accordance with the "law of the land".

Respectfully submitted,

EDWARD G. BUCKLAND
WILLIAM J. KANE
Attorneys for The Railroad Credit Corporation,
Respondent.

Dated: October 1, 1942.

APPENDIX A

ALLAN P. MATTHEW,
Balfour Building,
San Francisco, California

Filed Sept. 4, 1942
WALTER B. MALING, *Clerk*

IN THE DISTRICT COURT OF THE UNITED STATES,

FOR THE

NORTHERN DISTRICT OF CALIFORNIA,
SOUTHERN DIVISION

In the Matter of
THE WESTERN PACIFIC RAILROAD COMPANY, *Debtor.* } No. 26591–S

PETITION OF TRUSTEES FOR INSTRUCTIONS RESPECTING RETIREMENT BY REDEMPTION OF A PORTION OF THE PRINCIPAL AMOUNT OF INDEBTEDNESS REPRESENTED BY THEIR OUTSTANDING CERTIFICATES OF INDEBTEDNESS AND FOR AN ORDER AUTHORIZING A FURTHER EXTENSION OF EITHER ALL OR A PORTION OF SAID CERTIFICATES

T. M. SCHUMACHER and SIDNEY M. EHRMAN, the duly appointed and qualified Trustees of the properties of the Debtor above named, hereby petition the Court and represent as follows:

I.

Pursuant to authority duly given them by this Court with the approval of the Interstate Commerce Commission, your

petitioners, as such Trustees, heretofore issued their certificates of indebtedness in the principal amount of $10,000,000, maturing and payable on December 1, 1939. The said certificates were later extended as hereinafter shown. The said certificates were issued to evidence and secure a loan in the sum of $10,000,000 from the Reconstruction Finance Corporation. The Trustees borrowed the said sum of $10,000,000 from the Reconstruction Finance Corporation for the purpose of paying at maturity their certificates of indebtedness then outstanding and maturing and payable on December 1, 1938. The proceeds of said loan were used for said purpose. The said certificates then outstanding and maturing and payable on December 1, 1938, represented an indebtedness all of which was authorized and incurred for the purpose of meeting the cost of doing certain work upon and acquiring certain equipment for the railroad of the Debtor which it was necessary should be done and acquired in order that said railroad might be operated with safety and reasonable efficiency, that its physical elements might be conserved and its existing business retained, and that it might furnish to the public service in the way of transportation of persons and property adequately responsive to the reasonable requirements and demands of the public upon said railroad for such service. The proceeds realized by the incurrence of the indebtedness represented by said certificates were expended in the doing of said work and the acquiring of said equipment.

II.

Pursuant to authority duly given them by this Court, with the approval of the Interstate Commerce Commission, your petitioners, as such Trustees, extended said certificates of indebtedness from December 1, 1939, to December 1, 1940, to evidence and secure an extension of said loan from and to the same dates, and further extended said certificates from

December 1, 1940, to December 1, 1941, to evidence and secure a further extension of said loan from and to the same dates. Your petitioners were authorized by the order of this Court made on November 27, 1940, to obtain said further extension of said loan to December 1, 1941, from the Reconstruction Finance Corporation, upon an agreement by your petitioners with the Reconstruction Finance Corporation to curtail the principal of said loan by the amount of $12,500 on December 15, 1940, and by a like amount on the 15th day of each month thereafter during the term of said loan, so long as the said certificates, or any of them, should be held by the Reconstruction Finance Corporation. Pursuant to said order of November 27, 1940, your petitioners obtained from the Reconstruction Finance Corporation said further extension of said outstanding loan to December 1, 1941, and made and entered into said agreement with Reconstruction Finance Corporation. Pursuant to said order of November 27, 1940, and said agreement with the Reconstruction Finance Corporation, your petitioners curtailed the principal of said loan by the amount of $12,500 on the 15th day of the months of December, 1940, to November, 1941, both inclusive, thereby reducing the said principal of said loan to the total amount of $9,850,000, and the said Certificates of Indebtedness in said reduced principal amount were outstanding and held by Reconstruction Finance Corporation on December 1, 1941.

III.

Pursuant to authority duly given them by this Court, with the approval of the Interstate Commerce Commission, your petitioners, as such Trustees, further extended said Certificates of Indebtedness in the total principal amount of $9,850,000 from December 1, 1941, to December 1, 1942, to evidence and secure a further extension of said loan from and to the same dates. Your petitioners were authorized by

the order of this Court made on November 26, 1941, to obtain said further extension of said loan to December 1, 1942, from the Reconstruction Finance Corporation, upon an agreement by your petitioners with the Reconstruction Finance Corporation to curtail the principal of said loan by the amount of $25,000 on December 15, 1941, and by a like amount on the 15th day of each month thereafter during the term of said loan, so long as said Certificates of Indebtedness, or any of them, are held by the Reconstruction Finance Corporation. The said order of November 26, 1941, further authorized your petitioners to extend further to December 1, 1942, their said Certificates of Indebtedness then outstanding in the total principal amount of $9,850,000 as evidence of and security for said further extension of said loan, the said Certificates as further extended to bear interest at the rate of four per cent (4%) per annum, payable monthly, the same rate of interest as was borne by said certificates as previously extended, to be subject to a right of said Trustees, so long as said Certificates are held by the Reconstruction Finance Corporation, to redeem upon thirty (30) days' notice on any interest payment date such other of said certificates as they may desire as are not retired by said curtailment of the principal of said loan, and to be subject to a right of said Trustees, if said Certificates are no longer held by the Reconstruction Finance Corporation, to redeem upon thirty (30) days' notice all but not less than all of said Certificates on any interest payment date, and the said further extension to be effectuated by said Trustees by stamping or writing upon each of said outstanding certificates a legend or endorsement reading substantially as follows:

> "The holder hereof by acceptance hereof bearing hereon this endorsement hereby agrees that the maturity of the within certificate is further extended to December 1, 1942, with interest at the rate of 4% per annum

payable monthly, with the privilege of redemption by the Trustees of the within certificate so long as the same is held by the Reconstruction Finance Corporation and the privilege of redemption by the Trustees, if the within certificate is no longer held by the Reconstruction Finance Corporation, of all but not less than all of the Trustees' Certificates of this issue, in any event on any interest payment date on thirty days' previous notice at the principal amount and accrued interest to the date fixed for redemption.

"The Trustees agree to curtail the principal of the loan evidenced by the within certificate by the amount of $2500 on December 15, 1941, and by a like amount on the 15th day of each month thereafter during the term of this extension, so long as this certificate, or any of the certificates evidencing the loan referred to therein, shall be held by the Reconstruction Finance Corporation."

The Trustees were further authorized by said order of November 26, 1941, (1) to put up with the Reconstruction Finance Corporation, incidentally to the further extension of said loan to December 1, 1942, and as collateral security therefor, the sum of $5,000,000 from cash in the hands of said Trustees, interest upon said loan to be computed upon the outstanding balance of said loan less the amount of said cash collateral, and the said cash collateral to be subject to a right and privilege on the part of said Trustees to withdraw all or any part of said cash collateral at any time (but not less than $250,000 at any one time) upon an order of the Court, made with or without notice or hearing, instructing them to make such withdrawal, provided, however, that the Trustees shall give Reconstruction Finance Corporation at least ten (10) days' written notice of their intention to apply for any such order and, following the making of any such order, at least five (5) days' notice of the date on which withdrawal is to be made, and (2) to

put up with the Reconstruction Finance Corporation from time to time thereafter, as further collateral security aforesaid further extension of said loan and subject to the same terms and conditions, such additional amounts of cash as said Trustees may find and determine to be available for said purpose, and as Reconstruction Finance Corporation may be willing to accept upon such terms and conditions. Pursuant to said order of November 26, 1941, your petitioners, with the prior approval of the Interstate Commerce Commission, obtained from the Reconstruction Finance Corporation a further extension of said outstanding loan to December 1, 1942, and made and entered into an agreement with Reconstruction Finance Corporation to curtail the principal of said loan by the amount of $25,000 on December 15, 1941, and by a like amount on the 15th day of each month thereafter during the term of said loan, so long as the said certificates, or any of them, are held by the Reconstruction Finance Corporation, and effectuated said further extension by stamping upon each of said outstanding certificates a legend or endorsement in the form hereinbefore set forth. Your petitioners also put up with the Reconstruction Finance Corporation, incidentally to said further extension of said loan to December 1, 1942, and as collateral security therefor, the sum of $5,000,000 from cash in the hands of your petitioners, pursuant to said order. On April 24, 1942, your petitioners put up with Reconstruction Finance Corporation, as further collateral security for said loan and subject to the same terms and conditions, the additional sum of $1,000,000 from cash in the hands of your petitioners. Pursuant to said order of November 26, 1941, and said agreement by your petitioners with the Reconstruction Finance Corporation, your petitioners have curtailed the principal of said loan by the amount of $25,000 on the 15th day of the months of December, 1941, to August,

1942, both inclusive, thereby reducing the said principal of said loan to the total amount of $9,625,000, and the said Certificates of Indebtedness in said reduced principal amount are now outstanding and held by Reconstruction Finance Corporation and mature and are payable on December 1, 1942. Your petitioners have paid to Reconstruction Finance Corporation the interest upon the said outstanding Certificates of Indebtedness to and including the 1st day of September, 1942. Your petitioners will further curtail the principal of said loan by the amount of $25,000 on the 15th day of each of the months of September, October and November, 1942, thereby reducing the said principal of said loan to the total amount of $9,550,000.

IV.

A plan of reorganization of the Debtor was approved by order of this Court made on August 15, 1940. On September 20, 1940, appeals from said order to the Circuit Court of Appeals for the Ninth Circuit were filed by certain interested parties. The said appeals were argued before said Circuit Court of Appeals on July 28 and July 29, 1941, and briefs in said appeals were filed prior to said argument. On November 28, 1941, said Circuit Court of Appeals reversed said order of this Court made on August 15, 1940, and remanded said proceeding with directions to dismiss it or, in the Court's discretion and on motion of any party in interest, refer it back to the Interstate Commerce Commission for further action. Thereafter petitions for a writ of certiorari to said Circuit Court of Appeals were filed by certain interested parties with the Supreme Court of the United States. The said petitions were granted on April 27, 1942, and it is expected that said proceedings will be orally argued before the Supreme Court early during the term commencing in October, 1942.

V.

On March 27, 1941, your petitioners filed with this Court their petition that they be instructed whether they should retire, out of funds on hand, a portion of the principal amount of the indebtedness represented by their outstanding Certificates of Indebtedness and, if the Court should determine that such partial retirement of said indebtedness should be made, that your petitioners be instructed with respect to the amount thereof. On April 3, 1941, A. C. James Co., an intervenor in the above entitled reorganization proceeding, filed with this Court a motion for an order directing your petitioners to pay off and discharge out of any available cash of the Debtor in their hands not less than $3,000,000 of the principal indebtedness represented by said certificates, and directing your petitioners to report fully to the Court, for the information of all parties in interest, as to any and all negotiations which they might have had with private bankers or others during the preceding twelve months looking toward a refunding of said certificates. On April 22, 1941, said petition for instructions and said motion were jointly and fully heard before the Court and oral and documentary evidence was introduced, including the testimony of one of your petitioners. On May 13, 1941, the Court rendered its opinion and order upon said petition and motion. By said order of May 13, 1941, the Court instructed your petitioners not to make any payment on account of said Trustees' Certificates and not to make any further effort to refund them by the issue of new Trustees' certificates to others than the Reconstruction Finance Corporation. By said order the said motion of A. C. James Co. was denied. An appeal by A. C. James Co. from said order to the Circuit Court of Appeals for the Ninth Circuit was filed, briefs in said appeal were filed, and on July 29, 1941, the said appeal was submitted to said

Court without oral argument. On September 30, 1941, said Court dismissed said appeal upon the ground that said A. C. James Co. was not entitled to appeal. The said order of this Court made on May 13, 1941, remains in force and effect.

VI.

The orders of this Court authorizing the issuance and the extensions of said certificates of indebtedness now outstanding and, as extended, maturing and payable on December 1, 1942, and the orders of the Interstate Commerce Commission approving the issuance of said certificates expressly provide that said certificates rank as expenses of the administration by the Court of the Debtor's property and as such are payable in due course of administration equally with other expenses of administration out of said property and constitute a charge and direct first lien upon said property prior in right to the debts and obligations of the Debtor and to any lien created by it, and said certificates were issued by your petitioners for value upon the representation that such was their character.

VII.

Your petitioners had cash on hand as of September 1, 1942, in the total amount of $4,493,000 and they expect to have cash on hand as of December 1, 1942, after meeting all expenses to be incurred in the operation and maintenance of the properties of the Debtor, in the total amount of not less than $6,000,000. In addition thereto, as hereinbefore set forth, your petitioners have put up with the Reconstruction Finance Corporation the total amount of $6,000,000 incidentally to and as collateral security for said further extension of said loan. Petitioners are of the opinion that they would be able, without impairment of necessary work-

ing capital and without prejudice to the conduct of the railroad business of the Debtor, to retire by redemption out of cash on hand and said cash put up with the Reconstruction Finance Corporation a substantial portion of the principal amount of the indebtedness represented by said outstanding certificates of indebtedness. By reason of said increase in the amount of cash available to your petitioners, including said sums put up with and now held by the Reconstruction Finance Corporation, and said order of this Court made on May 13, 1941, your petitioners desire to receive instructions from this Court with respect to the partial retirement of said indebtedness and, if such partial retirement should be ordered by the Court, the amount thereof.

VIII.

In the event that the Court should determine that such partial retirement of the principal amount of the indebtedness represented by their outstanding certificates of indebtedness should not be made, it will be necessary for your petitioners to obtain a further extension of said loan and that they again extend said certificates as evidence of and security for said loan, in order to insure against a default upon the said certificates, and if the Court should determine that such partial retirement of said indebtedness should be made, it will likewise be necessary for your petitioners to obtain a further extension of the remaining portion of said loan and that they again extend the remaining portion of said certificates. Your petitioners believe that they can obtain a further extension of said loan or such portion thereof to December 1, 1943, from the Reconstruction Finance Corporation, the said further extension of said loan or such portion thereof to be evidenced and secured by a further extension of the said certificates of indebtedness or such portion thereof by your petitioners to December 1,

1943, with interest at the rate of four per cent (4%) per annum payable monthly, which is the same rate of interest as is borne by said certificates as previously thrice extended, and subject to a right on the part of the Trustees, so long as said certificates are held by the Reconstruction Finance Corporation, to redeem upon thirty (30) days' notice on any interest payment date such of said certificates as they may desire, and to be subject to a right of said Trustees, if said certificates are no longer held by the Reconstruction Finance Corporation, to redeem upon thirty (30) days' notice all but not less than all of the outstanding certificates on any interest payment date, the said further extension of said certificates to be effectuated by stamping or writing upon each of said certificates a legend or endorsement reading substantially as follows:

> "The holder hereof by acceptance hereof bearing hereon this endorsement hereby agrees that the maturity of the within certificate is further extended to December 1, 1943, with interest at the rate of 4% per annum payable monthly, with the privilege of redemption by the Trustees of the within certificate so long as the same is held by the Reconstruction Finance Corporation and the privilege of redemption by the Trustees, if the within certificate is no longer held by the Reconstruction Finance Corporation, of all but not less than all of the outstanding Trustees' Certificates of this issue, in any event on any interest payment date on thirty days' previous notice at the principal amount and accrued interest to the date fixed for redemption."

If the Court should determine that such partial retirement of said indebtedness should be made, it will be in the interest of the trust estate of your petitioners that they be authorized to obtain a further extension of said loan and to extend again said certificates as evidence of and security for said loan in order to insure against a default upon the said certificates when the principal thereof falls due on

December 1, 1942. If the Court should determine that such partial retirement of said indebtedness should be made, it will likewise be in the interest of the trust estate of your petitioners that they be authorized to obtain a further extension of the remaining portion of said loan and to extend again the remaining portion of said certificates. To consummate and fully authorize the said further extension of said loan or such portion thereof it will be necessary for your petitioners to make formal application for said further extension to the Reconstruction Finance Corporation and to secure the approval thereof by the Interstate Commerce Commission.

IX.

Because of the possibility that your petitioners may not be able to arrange with the Reconstruction Finance Corporation for said further extension of said loan or such portion thereof it is advisable that the Court, in its order granting the authority herein asked for, reserve jurisdiction to authorize, by supplemental order, made with or without notice, the issuance and sale by your petitioners of new certificates of indebtedness in the total amount of $9,550,000 or a portion thereof, dated December 1, 1942, and bearing interest at the rate of four per cent (4%) per annum or a different rate of interest, for the purpose of providing themselves with funds for the payment of said outstanding certificates or such portion thereof at maturity.

X.

For the purpose of meeting the requirements of Section 4 of Public Act No. 35 of the Seventy-Third Congress of the United States, approved June 10, 1933, it will be necessary, if said further extension of said loan or such portion thereof is made, for your petitioners to enter into a fourth

supplemental agreement with the Reconstruction Finance Corporation substantially in the form attached hereto and marked Exhibit "A".

WHEREFORE, your petitioners pray:

(1) That upon the filing of this petition the Court set the same for hearing and prescribe the notice to be given thereof.

(2) That upon the hearing of said petition your petitioners be instructed whether they should retire by redemption, out of funds on hand and said cash put up with the Reconstruction Finance Corporation, a portion of the principal amount of the indebtedness represented by their outstanding Certificates of Indebtedness and, if the Court should determine that such partial retirement of said indebtedness should be made, that petitioners be instructed with respect to the amount thereof.

(3) That pursuant to and in accordance with said instructions the Court authorize your petitioners to apply forthwith to the Reconstruction Finance Corporation for a further extension of said loan or the remaining portion thereof to December 1, 1943, and to the Interstate Commerce Commission for its approval thereof, and to make such other application or supplemental applications to the Interstate Commerce Commission as may be required in respect to said further extension of said outstanding certificates of indebtedness or remaining portion thereof.

(4) That pursuant to and in accordance with said instructions the Court make its order whereby your petitioners will be authorized to extend further to December 1, 1943, their outstanding certificates of indebtedness in the total amount of $9,550,000, or the remaining portion thereof, as evidence of and security for the said further extension of said loan or the remaining portion thereof, the said certificates as again extended to bear interest at the rate of four

per cent (4%) per annum payable monthly, the same rate of interest as is borne by said certificates as previously extended, and to be subject to a right of the Trustees, so long as said certificates are held by the Reconstruction Finance Corporation, to redeem upon thirty (30) days' notice on any interest payment date such of said certificates as they may desire, and to be subject to a right of said Trustees, if said certificates are no longer held by said Reconstruction Finance Corporation, to redeem upon thirty (30) days' notice all but not less than all of said certificates on any interest payment date, and the said further extension to be effectuated by the Trustees by stamping or writing upon each of said certificates a legend or endorsement reading substantially as follows:

> "The holder hereof by acceptance hereof bearing hereon this endorsement hereby agrees that the maturity of the within certificate is further extended to December 1, 1943, with interest at the rate of 4% per annum payable monthly, with the privilege of redemption by the Trustees of the within certificate so long as the same is held by the Reconstruction Finance Corporation and the privilege of redemption by the Trustees, if the within certificate is no longer held by the Reconstruction Finance Corporation, of all but not less than all of the outstanding Trustees' Certificates of this issue, in any event on any interest payment date on thirty days' previous notice at the principal amount and accrued interest to the date fixed for redemption."

provided, however, that the Court reserve jurisdiction to provide by supplemental order, made with or without notice, that with the approval of the Interstate Commerce Commission first had and obtained the Trustees may issue and sell new certificates of indebtedness in the total amount of $9,550,000 or a portion thereof, dated December 1, 1942, and bearing interest at the rate of four per cent (4%) per

annum or a different rate of interest, for the purpose of meeting the principal of the outstanding certificates or the remaining portion thereof at maturity.

(5) That your petitioners be further authorized by such order to make a fourth supplemental agreement with the Reconstruction Finance Corporation substantially in the form attached hereto and marked Exhibit "A".

(6) That your petitioners be authorized (1) to put up with the Reconstruction Finance Corporation, incidentally to the further extension of said loan or the remaining portion thereof to December 1, 1943, and as collateral security therefor, such amount of cash, if any, as your petitioners may find and determine to be available for said purpose and as the Reconstruction Finance Corporation may be willing to accept, interest upon said loan or said portion thereof to be computed upon the outstanding balance of said loan or said portion thereof less the amount of said cash collateral, and the said cash collateral to be subject to a right and privilege on the part of said Trustees to withdraw all or any part of said cash collateral at any time (but not less than $250,000 at any one time) upon an order of the Court, made with or without notice or hearing, instructing them to make such withdrawal, provided, however, that the Trustees shall give Reconstruction Finance Corporation at least ten (10) days' written notice of their intention to apply for any such order and, following the making of any such order, at least five (5) days' notice of the date on which withdrawal is to be made; (2) to put up with the Reconstruction Finance Corporation from time to time thereafter, as further collateral security for said further extension of said loan or such portion thereof and subject to the same terms and conditions, such additional amounts of cash, if any, as said Trustees may find and determine to be available for said purpose, and as Reconstruction Finance

Corporation may be willing to accept upon such terms and conditions; and (3) to enter into an agreement with the Reconstruction Finance Corporation substantially in the form attached hereto and marked Exhibit "B", and to enter into similar agreements in the event that said additional amounts of cash shall be put up with the Reconstruction Finance Corporation.

ALLAN P. MATTHEW,
Counsel for Petitioners.

STATE OF CALIFORNIA }
City and County of San Francisco } *ss.*

CHARLES ELSEY, being first duly sworn, deposes and says:

That for more than ten years last past he has been the President of The Western Pacific Railroad Company and, since the appointment of the Trustees of the properties of said Company, he has been their Agent in immediate charge of the railroad and other property of that Company; that he has read the foregoing petition and knows the contents thereof and the same is true of his own knowledge.

CHARLES ELSEY

Subscribed and sworn to before me
this 4th day of September, 1942.

MARY N. WICKERSHAM [SEAL]
Notary Public
in and for the City and County of
San Francisco, State of California

EXHIBIT "A"

December ....., 1942.

Reconstruction Finance Corporation,
Washington, D. C.

Fourth Supplemental Agreement

Dear Sirs:

The undersigned Trustees of The Western Pacific Railroad Company are indebted to your corporation on account of a certain loan represented by Trustees' Certificates in the principal amount of $....., which, as extended, mature on December 1, 1942.

In consideration of the granting by your corporation of a fourth extension of the maturity date of the above mentioned Trustees' Certificates, authorized by supplemental report and supplemental order of the Interstate Commerce Commission dated ...., 1942, in Finance Docket No....., the undersigned Trustees, as such and not individually, hereby agree with your corporation as follows:

1. The term "compensation" as used in this fourth supplemental agreement shall include all salaries, fees, bonuses, commissions or other payments, direct or indirect, in money or otherwise, for personal services.

2. So long as they are indebted to your corporation the undersigned Trustees will not increase the compensation of any of their officers, directors or employees to any amount not permitted by the terms of the agreement dated November 23, 1938, the supplemental agreement dated December 1, 1939, the second supplemental agreement dated December 2, 1940, and the third supplemental agreement dated December 1, 1941, between your corporation and the undersigned Trustees, and in any written consents given by your corporation pursuant to the provisions of said agreement and supplemental agreements.

3. The undersigned Trustees hereby ratify, confirm and reaffirm the said agreement of November 23, 1938, the said supplemental agreement of December 1, 1939, said second supplemental agreement of December 2, 1940, and said third supplemental agreement dated December 1, 1941, and

each and every covenant contained in said agreement and supplemental agreements.

Respectfully submitted,

.....

.....

As Trustees of
THE WESTERN PACIFIC
RAILROAD COMPANY

Attest:

.....

Agent for the Trustees of
THE WESTERN PACIFIC
RAILROAD COMPANY

EXHIBIT "B"

AGREEMENT

THIS AGREEMENT, made and entered into this ..... day of ....., 1942, by and between T. M. SCHUMACHER and SIDNEY M. EHRMAN, as Trustees in Reorganization of The Western Pacific Railroad Company, and not individually, hereinafter referred to as the Trustees, and RECONSTRUCTION FINANCE CORPORATION,

WITNESSETH:

WHEREAS, the Trustees are indebted, as such Trustees, to Reconstruction Finance Corporation on account of a certain loan represented by Trustees' Certificates in the principal amount of $....., which, as extended, mature on December 1, 1942, and

WHEREAS, pursuant to approval by the Interstate Commerce Commission by its supplemental report and certificate dated ...., 1942, in Finance Docket No....., the Reconstruction Finance Corporation has granted an extension of said loan to December 1, 1943, and

WHEREAS, the Trustees desire to put up, and the Reconstruction Finance Corporation is willing to accept, as col-

lateral security for said loan, the sum of $.....,
subject to the terms and conditions hereinafter set forth;

NOW, THEREFORE, in consideration of the premises, IT IS HEREBY MUTUALLY AGREED AND UNDERSTOOD by and between the Trustees and Reconstruction Finance Corporation as follows:

1. Interest upon said loan shall be computed upon the outstanding balance of said loan less the amount of the said cash collateral.

2. The said cash collateral shall be subject to a right and privilege on the part of the Trustees to withdraw all or any part of said collateral at any time (but not less than $250,000 at any one time) upon an order of the District Court of the United States, for the Northern District of California, Southern Division made with or without notice or hearing, in the proceeding pending in said Court and entitled In the Matter of The Western Pacific Railroad Company, Debtor, No. 26591–S, and instructing the Trustees to make such withdrawal; provided, however, that the Trustees shall give Reconstruction Finance Corporation at least ten days' written notice of their intention to apply for any such order and, following the making of any such order, at least five days' notice of the date on which withdrawal is to be made.

3. The Trustees shall have the right to put up with Reconstruction Finance Corporation from time to time, as further collateral security for said loan and subject to the same terms and conditions, such additional sums as the Trustees may find and determine to be available for said purpose, and as Reconstruction Finance Corporation may be willing to accept upon such terms and conditions.

IN WITNESS WHEREOF, the parties have executed this agreement the day and year first above written.

.....

.....

As Trustees in Reorganization of
THE WESTERN PACIFIC RAILROAD COMPANY

RECONSTRUCTION FINANCE CORPORATION
By .....

.....

ALLAN P. MATTHEW,
1500 Balfour Building,
San Francisco, California

Filed Sept. 4, 1942
WALTER B. MALING, *Clerk*

IN THE DISTRICT COURT OF THE UNITED STATES,
FOR THE
NORTHERN DISTRICT OF CALIFORNIA,
SOUTHERN DIVISION

In the Matter of
THE WESTERN PACIFIC RAILROAD COMPANY,
Debtor.
No. 26591-S

ORDER PROVIDING FOR HEARING UPON PETITION OF TRUSTEES FOR INSTRUCTIONS RESPECTING RETIREMENT BY REDEMPTION OF A PORTION OF THE PRINCIPAL AMOUNT OF INDEBTEDNESS REPRESENTED BY THEIR OUTSTANDING CERTIFICATES OF INDEBTEDNESS AND FOR AN ORDER AUTHORIZING A FURTHER EXTENSION OF EITHER ALL OR A PORTION OF SAID CERTIFICATES

Upon due consideration of the petition of T. M. SCHUMACHER and SIDNEY M. EHRMAN, Trustees of the properties of the Debtor above named, filed herein and praying for instructions with respect to the retirement by redemption of a portion of the principal amount of indebtedness represented by their outstanding certificates of indebtedness in the amount of $9,550,000 and for an order authorizing the further extension of either all or a portion of said

certificates of indebtedness, IT IS HEREBY ORDERED as follows:

1. That said petition shall be and it hereby is set for hearing before this Court on September 28, 1942, at 10:00 o'clock, A.M.

2. That said Trustees be and they hereby are directed to give notice of the said hearing. That said notice be given by (a) publication on or before September 10, 1942, of a notice substantially in the following form in The Wall Street Journal (Pacific Coast Edition) and The Recorder, two newspapers of general circulation published in the City and County of San Francisco, State of California:

LEGAL NOTICE

IN THE DISTRICT COURT OF THE UNITED STATES

FOR THE

NORTHERN DISTRICT OF CALIFORNIA,
SOUTHERN DIVISION

In the Matter of THE WESTERN PACIFIC RAILROAD COMPANY, *Debtor.*	No. 26591-S

Notice of Hearing upon Petition of Trustees for Instructions Respecting Retirement by Redemption of a Portion of the Principal Amount of Indebtedness represented by their Outstanding Certificates of Indebtedness and for an Order authorizing a further extension of either all or a portion of said Certificates

NOTICE IS HEREBY GIVEN, pursuant to the order of the above named court, that a hearing will be held before

the Honorable A. F. St. Sure, Judge of the above entitled court, at the court room of the said Judge, in the United States Post Office and Court House Building, Seventh and Mission Streets in the City and County of San Francisco, State of California, on September 28, 1942, at 10 o'clock, A.M., or as soon thereafter as the same may be heard, upon the petition of T. M. Schumacher and Sidney M. Ehrman, Trustees in Reorganization of The Western Pacific Railroad Company, praying:

(1) That they be instructed whether they should retire by redemption, out of funds on hand and cash put up with the Reconstruction Finance Corporation as collateral security for a loan to said Trustees, a portion of the principal amount of the indebtedness represented by their outstanding certificates of indebtedness and, if the Court should determine that such partial retirement of said indebtedness should be made, that petitioners be instructed with respect to the amount thereof.

(2) That pursuant to and in accordance with said instructions the Court authorize said Trustees to apply forthwith to the Reconstruction Finance Corporation for a further extension of said loan or the remaining portion thereof from December 1, 1942, to December 1, 1943, and to the Interstate Commerce Commission for its approval thereof, and to make such other application or supplemental applications to the Interstate Commerce Commission as may be required in respect to said further extension of said outstanding certificates of indebtedness or remaining portion thereof.

(3) That pursuant to and in accordance with said instructions the Court make its order whereby said Trustees will be authorized to extend further from December 1, 1942, to December 1, 1943, their outstanding certificates of indebtedness in the total amount of $9,550,000, or the remaining portion thereof, as evidence of and security for the said further extension of said loan or the remaining portion thereof, the said certificates as again extended to bear interest at the rate of four per cent (4%) per annum payable monthly, the same rate of interest as is borne by said certificates as previously extended, and to be subject to a right of the Trustees, so long as said certificates are held by the

Reconstruction Finance Corporation, to redeem upon thirty (30) days' notice on any interest payment date such of said certificates as they may desire, and to be subject to a right of said Trustees, if said certificates are no longer held by said Reconstruction Finance Corporation, to redeem upon thirty (30) days' notice all but not less than all of said certificates on any interest payment date, and the said further extension to be effectuated by the Trustees by stamping or writing upon each of said certificates a legend or endorsement reading substantially as follows:

> "The holder hereof by acceptance hereof bearing hereon this endorsement hereby agrees that the maturity of the within certificate is further extended to December 1, 1943, with interest at the rate of 4% per annum payable monthly, with the privilege of redemption by the Trustees of the within certificate so long as the same is held by the Reconstruction Finance Corporation and the privilege of redemption by the Trustees, if the within certificate is no longer held by the Reconstruction Finance Corporation, of all but not less than all of the outstanding Trustees' Certificates of this issue, in any event on any interest payment date on thirty days' previous notice at the principal amount and accrued interest to the date fixed for redemption."

provided, however, that the Court reserve jurisdiction to provide by supplemental order, made with or without notice, that with the approval of the Interstate Commerce Commission first had and obtained the Trustees may issue and sell new certificates of indebtedness in the total amount of $9,550,000 or a portion thereof, dated December 1, 1942, and bearing interest at the rate of four per cent (4%) per annum or a different rate of interest, for the purpose of meeting the principal of the outstanding certificates or the remaining portion thereof at maturity.

(4) That said Trustees be further authorized by such order to make a Fourth Supplemental Agreement with Reconstruction Finance Corporation substantially in the form attached to said petition and marked Exhibit "A".

(5) That said Trustees be authorized (1) to put up with the Reconstruction Finance Corporation, incidentally to the further extension of said loan or the remaining portion thereof to December 1, 1943 and as collateral security therefor, such amount of cash, if any, as said Trustees may find and determine to be available for said purpose and as the Reconstruction Finance Corporation may be willing to accept, interest upon said loan or said portion thereof to be computed upon the outstanding balance of said loan or said portion thereof less the amount of said cash collateral, and the said cash collateral to be subject to a right and privilege on the part of said Trustees to withdraw all or any part of said cash collateral at any time (but not less than $250,000 at any one time) upon an order of the court, made with or without notice or hearing, instructing them to make such withdrawal, provided, however, that the Trustees shall give Reconstruction Finance Corporation at least ten (10) days' written notice of their intention to apply for any such order and, following the making of any such order, at least five (5) days' notice of the date on which withdrawal is to be made; (2) to put up with the Reconstruction Finance Corporation from time to time thereafter, as further collateral security for said further extension of said loan or such portion thereof and subject to the same terms and conditions, such additional amounts of cash, if any, as said Trustees may find and determine to be available for said purpose, and as Reconstruction Finance Corporation may be willing to accept upon such terms and conditions; and (3) to enter into an agreement with the Reconstruction Finance Corporation substantially in the form attached to said petition and marked Exhibit "B" and to enter into similar agreements in the event that said additional amounts of cash shall be put up with the Reconstruction Finance Corporation.

T. M. SCHUMACHER
SIDNEY M. EHRMAN
Trustees in Reorganization of The Western Pacific Railroad Company.

and (b) by mailing prior to September 11, 1942, a copy of this order and of said petition to the following parties:

1. Crocker First National Bank of San Francisco and Samuel Armstrong.
2. Irving Trust Company, as Trustee under Indenture securing Debtor's General and Refunding Mortgage Bonds.
3. A. C. James Co.
4. Reconstruction Finance Corporation.
5. The Railroad Credit Corporation.
6. The Chase National Bank of the City of New York, as Trustee under agreement dated May 1, 1929, covering Equipment Trust Certificates.
7. The Western Pacific Railroad Company.
8. The Western Pacific Railroad Corporation.
9. The Western Realty Company.
10. Central Hanover Bank and Trust Company, as Trustee under agreement dated February 1, 1937, covering Equipment Trust Certificates.
11. Central Hanover Bank and Trust Company, as Trustee under agreement dated August 1, 1941, covering Equipment Trust Certificates.

Dated: September 4, 1942.

A. F. St. Sure,
Judge.